

# Foreign Agricultural Service *GAIN* Report

Global Agriculture Information Network

Required Report - public distribution

GAIN Report #BR2611

Date: 8/30/2002

# **Brazil**

# **Poultry and Products**

# Annual

2002

Approved by:

William W. Westman, Agricultural Counselor U.S. Embassy

Prepared by:

Joao F. Silva, Agricultural Specialist

## **Report Highlights:**

After several years of record growth in production and exports, the broiler outlook in 2003 calls for a slowdown in production and a drop in exports. Increased feed costs have trimmed profits for both producers and packers. Turkey production and exports continue to climb but from a small base.

Executive Summary	1
Commodity Outlook, Broilers	1
Production	1
Production Factors	2
Production Costs	2
Consumption	3
Trade	
Stocks	5
Policy	5
Marketing	6
Commodity Outlook, Turkey	
Production	
Consumption	8
Trade	
PSD Tables	9
Poultry Meat, Chicken - 16 wks	
Poultry meat, Turkey	

GAIN Report #BR2611 Page 1 of 11

## **Executive Summary**

The current economic indicators suggest a weakening of the Brazilian economy in the second half of 2002, although there are sectors of the economy that are doing quite well such as the export sector with an estimated US\$6 billion surplus in the balance of trade and the agricultural sector with record crop and livestock production. However, the overall growth of the economy has been reduced to about one percent; unemployment is above 7 percent, domestic purchasing power suffers because real wages are expected to fall for the fourth successive year, and inflation of around 8 to 9 percent is twice projected levels for 2002. The devaluation of the Brazilian currency, the Real, reached 48 percent during Jan-July 2002, and continues to fluctuate in August despite the recently signed Brazil-IMF agreement of US\$30 billion. Much of these uncertainties derive from concerns of the international financial market about Brazil's capacity to roll over the large external debt of US\$ 210 billion, most of which is held by the private sector, and the ability to manage the large domestic debt. These uncertainties are fueled by the proximity of the October Presidential elections. The full electoral ballot will also include every seat in House (Camara), two-thirds of the Senate, and all state governors and representatives.

The impact of these economic conditions on the poultry sector is mixed. Although production and exports are growing, there are concerns about lower profit margins for producers due to higher feed costs. The devaluation of the Real helps the competitiveness of Brazilian products in overseas markets. However, the volatility of the exchange rate also increases input costs such as vaccines and soybean meal, which is quoted in dollars, and limits the availability of export credit financing for Brazilian poultry exporters. In addition, Brazilian exporters will face higher import tariffs in the European Union, which is expected to affect 80 percent of Brazil's broiler parts exports to that market. As a result, exporters are aggressively seeking new export markets to support the sector in 2003.

## **Commodity Outlook, Broilers**

#### **Production**

The outlook for broiler production in 2003 calls for a continued increase in output, but at a smaller rate than previous years. The increase in production reflects maturing investments in productive capacity by major poultry packers and higher domestic demand. However, higher production costs due to high prices of corn (because of lower corn crop) and soybean meal (because of the devaluation of the Real) are affecting the profit margins of producers and packers. In addition, projected lower broiler parts exports to the European Union are contributing to a contraction in 2003.

During Jan-Jun 2002, broiler production increased by nearly 17 percent, compared to the same period in 2001. The increase in production was fueled by the optimism of the sector in 2001 with growing exports, firm domestic demand, and profitable margins. However, the situation in 2002 is different with lower exports than initially projected, higher domestic stocks, and higher costs of production. This situation forced poultry producers in Southern Brazil, which accounts for 70 percent of the national broiler output, to reduce placements of broiler parent stocks by 11 percent.

GAIN Report #BR2611 Page 2 of 11

#### **Production Factors**

Nearly 98 percent of the poultry meat produced in Brazil is broiler meat, with the balance coming mainly from turkey production which is increasing rapidly but from a small base. According to trade sources, about 57 percent of the estimated broiler meat production in 2002 will consist of broiler parts and 43 percent of whole broilers. This is the result of a strategy adopted by the large broiler processors in Brazil to add value to their products in order to increase their profit margins and shift away from a "commodity" type of product, such as whole broilers. These companies produce whole broilers to meet demand from the export market, such as Saudi Arabia which prefers whole birds. The two top Brazilian poultry producers, Sadia and Perdigao, have developed sophisticated processed food product lines which include not only various poultry meat cuts but also prepared poultry, pork, and fish-based dishes.

The following table provides an overview of the production of parent stock and day-old chicks in Brazil:

	Parei	nt Stock	
Year	Layers (1,000)	Broilers (1,000)	Broiler Chicks (1,000)
1995	58,250	22,068	2,537,191
1996	56,002	21,773	2,593,094
1997	52,074	23,115	2,863,797
1998	56,513	25,058	2,858,645
1999	61,032	29,132	3,153,500
2000	60,949	27,536	3,254,100
2001	63,606	28,597	3,473,600
2002 (a)	68,330	30,885	3,767,970

a) Estimate

#### **Production Costs**

Although Brazilian poultry companies do not release production cost information, there are some representative costs supplied by trade sources. During the first half of 2002, the estimated average cost of broiler production reached US\$0.39 per kilogram, live weight (about US\$0.18per pound), up from an estimated cost of US\$0.38 per kilogram, live weight (about US\$0.17 per pound) from the same period of 2001. These prices in dollars are based on an average exchange rate of R\$2.43 per dollar during Jan-Jun 2002, and R\$2.15 per dollar during Jan-Jun 2001, which implies an increase in the exchange rate of 13 percent. The exchange rate as of August 28, 2002 was R\$3.11 per dollar.

GAIN Report #BR2611 Page 3 of 11

Feed costs are higher this year compared to last year. The price of corn increased by 54 percent during Jan-Jun 2002, compared to the same period last year. The increase in corn prices reflects the projected reduction in corn area during the 2002/03 crop year (Oct/Sep), because many corn producers are switching to soybeans, to improve profitability. Also, the price of soybean meal increased 25 percent during Jan-Jun 2002, compared to the same period in 2001, because of the devaluation of the Real. The price of soybeans and products are quoted in dollars. In addition, the devaluation of the Real also increased the cost of importing vaccines and other inputs.

Higher feed costs during 2002/03 crop year will likely have a greater impact on small and medium-sized poultry producers, because the large Brazilian poultry packers are introducing a mechanism normally used to assist soybean producers in financing their production costs. This mechanism is called a "advance purchasing contract", by which a large packer will pay the corn grower in advance a negotiated price for corn to guarantee a corn supply. In addition, the federal government is also introducing the "option sales contract" to corn growers as a tool to avoid a major drop in the area planted to corn during the 2002/03 crop year. The federal government through CONAB offers a futures price, normally between harvest periods, for the purchase of eligible crops (wheat, corn, rice, and cotton). The futures price is established by CONAB at the moment the contract is offered, and the price is always above the minimum price. The producer may acquire a product option to sell contracts of 27 metric tons. The producer of the option contract acquires the right to sell the contracted product to CONAB at a later date and price specified in the contract.

Sao Paulo: broiler production costs and whole sale prices for broilers (RTC), corn, and soybean meal:

Year	Broiler Cost	Wholesale Prices					
(US\$/KG/Live Weight)		Live Weight (US\$/KG)	RTC (US\$/KG)	Corn (US\$/60/KG)	Soybean Meal (US\$/KG)		
1995	0.63	0.62	1.58	8.16	0.17		
1996	0.60	0.69	1.56	9.00	0.26		
1997	0.59	0.62	1.44	7.58	0.28		
1998	0.61	0.66	0.93	8.27	0.17		
1999	0.59	0.44	0.63	6.21	0.15		
2000	0.47	0.50	0.68	7.78	0.18		
2001	0.38	0.41	0.53	4.64	0.19		
Jan-Jun 2002	0.39	0.42	0.54	6.07	0.21		

Source: Trade. RTC = Ready to Cook

#### Consumption

Domestic broiler consumption is projected to increase moderately in 2003 by three percent compared to this year.

GAIN Report #BR2611 Page 4 of 11

This reflects the firm demand from the food service industry, such as frozen chicken meals, pre-cooked meals, and chicken burgers. In addition, broiler meat is more competitive compared to beef and pork and more affordable to lower income consumers.

There are no statistics on the composition of domestic broiler consumption between whole birds and parts. However, Brazilian consumers still have an overwhelming preference for large whole broilers because of the large size of the lower income consumer group that cannot afford to buy beef. However, the structure of broiler demand is changing in Brazil according to some market analysts. Since the economic stabilization in late 1994, there has also been a shift in consumption toward more highly processed broiler products, mostly among the Brazilian middle and upper classes. The traditional diet staples, rice and dried beans, are losing ground to animal protein products such as poultry and dairy products. Large Brazilian poultry processors are responding to these changes by shifting their sales mix strategies toward broiler parts (mostly leg quarters and breast meat) and further processed value-added branded products, such as frozen chicken meals, pre-cooked meals, chicken nuggets, and chicken burgers. The institutional, food service, and fast food markets also offer great potential for Brazilian firms. Tailoring products to these sectors' needs is key to the processors' new strategies.

#### **Trade**

Post projects broiler exports in 2003 to drop by 4 percent in volume, because of the following factors: First, excess of chicken meat in the world market, which already caused a drop of 13 percent in Brazil's average export price during Jan-Jun 2002, compared to the same period last year. Second, the increase in the import tariff in the European Union for Brazilian broiler parts from 15.4 to 70 percent, because of the change in the salt content for parts from 1.2-1.5 to 1.9 percent. The change in the salt content forced the European Union officials to change the HTS category of Brazilian broiler parts. As a result, beginning October 1, 2002 Brazilian exporters will pay a 70 percent import tariff for broiler parts. This measure will affect 85 percent of all Brazilian exports to the European Union. Third, uncertainty with exports to the Russian market in 2003 because Brazilian trade sources believe that Russian officials will eventually impose import quotas and higher import tariffs, which will likely cut Brazilian exports to Russia by 50 percent.

During Jan-Jun 2002, Broiler exports increased in volume by only 3.9 percent, while the value exported dropped by 9.5 percent, compared to the same period last year. The average export price dropped from US\$1,078 in 2001 to US\$943 per metric ton, during Jan-Jun 2002.

Brazil-Canada Poultry Agreement. According to the Ministry of Agriculture, Livestock, and Food Supply (MAPA), Brazilian and Canadians officials signed a "sanitary equivalency agreement" on July 19, 2002, by which Brazil will sell to the Canadian market mostly fresh/frozen broiler chest and turkey meat, while the Canadians have the option to sell to Brazil chicken leg-quarters. According to trade sources, Brazilian exporters may export to Canada between 20,000 and 25,000 metric tons of broiler and turkey meat in the next 12 months. The agreement became effective August 1, 2002. Canada approved imports of Brazilian broiler and turkeys only from areas where Newcastle disease has been eradicated, which includes 9 states in the center-south regions of the country.

Brazil-Argentina Dispute on Minimum Import Price. After losing its case against Argentina in the MERCOSUL Court of Appeal, Brazil decided to request the opening of a panel at the WTO against the Argentine Government because of Resolution Number 574/2000 issue by the Argentine Ministry of the Economy (see Gain Report BR 0615). This

GAIN Report #BR2611 Page 5 of 11

resolution established minimum import prices for Brazilian poultry exports to Argentina.

Brasil-Saudi Arabia. The Brazilian Government reacted strongly against a Saudi Arabian poultry producer that accused France (and included Brazil in the list) of dumping poultry products in that country. According to the Brazilian Government, Saudi Arabia maintains high import tariffs on poultry. Brazilian exporters claim that Brazil should not be included in the same list as France, because Brazil does not subsidize its poultry exports. The Saudis also accused Brazilian poultry exporters of exporting broilers with a higher "water content" of 13 percent, while the international level of acceptance is 6 percent. The information provided by the Brazilian government says that the level of "water content" in Brazil is 5 percent. According to our sources, Brazil has a market share of 75 percent of Saudi Arabia's poultry imports. Brazilian Meat inspection officials are also complying with the requirement of the Saudi Arabian Government that "the chickens have not been fed with feed containing animal protein, fats, or ruminants."

Brazil-China Sanitary Agreement. The Ministry of Agriculture, Livestock, and Food Supply (MAPA) officially announced on August 9, 2002 a "Sanitary Equivalence Agreement" with China to allow beef and poultry exports to that country. On the reverse side, Brazil will allow imports of wheat, apple, pears, and animal products from China. Beef exports to China are allowed only from 12 states which are free of FMD with vaccination. A Chinese veterinary team visited several meat packers in Brazil during early August and a list of meat plants was approved for exports. Brazilian exporters expect to begin exports to China in September after the visit of a Brazilian Ministry of Agriculture team to China.

Brasil-Russia. During the outbreak of Foot-and-Mouth Disease (FMD) in the state of Rio Grande do Sul in May 2001, Russia suspended temporarily imports of poultry from that state. According to local government sources, Russia reestablished imports of poultry from that state as of August 8, 2001.

GMO Corn. Planting and commercial sale of GMO corn is still prohibited in Brazil. Because of the excellent corn crop in 2001, poultry producers did not face any problems with imported corn as they did in 2000. Imports of GMO corn remains prohibited, but may enter for feed use, if authorized by the federal court.

#### **Stocks**

Brazilian poultry processors work on a very short slaughter schedule and hold stocks only to meet export contracts. There are no government-owned chicken meat stocks.

#### **Policy**

There have been no changes in poultry production policy since our 2001 annual report. The poultry sector outlined its policy goals late in 1997 through a document called the "Brasilia Letter", in which, leading poultry producers requested from the Brazilian government the following policies and/or actions:

- a) strengthening Animal Health and Inspection Services, including the implementation of the new National Poultry Inspection Program (PNSA) in 1999;
- b) restructuring of taxes on agricultural inputs, including exemption from the state ICMS, similar to a value-added tax;
- c) infrastructure (road and storage facility) improvement programs aimed at reducing the cost of transporting and storing grains;

GAIN Report #BR2611 Page 6 of 11

d) establishment of new production financing and export credit programs for the poultry and pork sectors; and,

e) support from the government in multilateral negotiations to combat subsidies and protectionist measures by competitors and importing countries abroad.

The National Bank for Economic and Social Development (BNDES) provides meat packing houses (meat plants) subsidized long-term loans to build or modernize their meat packing houses. BNDES does not provide the loan directly to the producer or packer, but through other state and commercial private banks. Total funds allocated under BNDES for the livestock sector is estimated at US\$200 million in 2002. BNDES also offers the following programs aimed at financing exports, which are used by meat packers:

(1) ACC - Advance on Export Contracts and ACE - Advance of Exchange Delivered:

These programs represent an alternative for exporters to reduce the financial costs of their export operations. ACC enables an exporter to obtain a cash advance based on his export contract, prior to shipment of the product, while ACE is a cash advance after shipment of the product. Repayment terms are 180 days before or after shipment of the products. The cost to the exporters of obtaining ACC or ACE advances is equal to the international cost of financing exports (LIBOR plus a spread), now approximately 12 percent.

There are several ways of combining ACC with other export credit programs, but the two most important for agricultural and food exports are:

- ACC+PROEX. This program combines the benefits of ACC and PROEX programs described above.
  Established through Circular 2,825 of the Central Bank of Brazil on June 24, 1998, the program is mostly used by exporters of high-value food products or processed agricultural commodities.
- ACC + RURAL. This program allows exporters of coffee and soybeans to obtain cash advances
  (ACC) on their exports from the Bank of Brazil, using as collateral the Rural Promissory Note (CPR).
  The cash advance is limited to 50 percent of the export value of the shipment.

#### (2) BNDES-Exim:

The main objective of this program is to expand Brazilian exports in general, including agricultural commodities, by making three types of credit lines available to the exporters at costs competitive with international financing. The most widely used line of credit is similar to a buyer's or supplier's credit. Financing covers 100 percent of the shipment and repayment terms vary between 181 days to 12 years with interest rates based on LIBOR plus a spread. This program is also referred as the Brazilian "Eximbank" within BNDES. The amount allocated for this program in 2002 is US\$3.4 billion, of which meat plants (including poultry) may take up to US\$600 million.

#### Marketing

The Brazilian Poultry Exporters Association (ABEF) is a private, non-profit organization formed by the largest poultry processors and exporters. ABEF has similar goals and programs compared to the U.S. Poultry and Egg Export Council (USAPEEC). ABEF has worked in the past as a national lobbying group for poultry exporters with program activities aimed at the Brazilian government, international organizations, and foreign governments to guarantee market

GAIN Report #BR2611 Page 7 of 11

access and reduction of non-tariff barriers for Brazilian broiler exports. The five largest poultry exporters account for nearly 90 percent of all poultry exports from Brazil, and the two leading poultry processors - SADIA and PERDIGAO account for 51 percent of all poultry exports. These two companies formed an international company called Brazilian Food (BRF) Trading Company in early 2001 to export poultry (and pork) to specific markets overseas. The new trading company is equally owned by the two processors. Targeted countries to share their market promotion efforts, logistics, and sales include: Russia, Egypt, South Africa, Angola, Cuba, Dominican Republic, Iran, Iraq, and Jordan.

BRF Trading is based on the Italian market promotion model of "export consortium", by which producers, processors, packers, or companies form "partnerships" to explore specific export markets by sharing market promotion and logistical costs. Although the Brazilian government is promoting this type of consortium among different Brazilian sectors of the economy, there is no specific budget allocated to BRF under the APEX program. However, these two processors benefit from ABEF's market promotion program.

ABEF was one of the first private organizations to implement its export promotion together with the federal government's market promotion agency - APEX. Since 2000, ABEF has participated in several trade shows overseas, mostly in Europe, Asia, and the Middle East. Promotion activities include demonstrations and in store promotions, general media activity, and market research. Although not similar to FAS's market promotion programs, ABEF includes several market access activities such as eliminating sanitary barriers and conducting trade servicing, under the budget for market promotion. ABEF's 2002 budget for market promotion is estimated at US\$2.5 million, of which APEX funds 43 percent (US\$1.1 million).

In 2002, the ten largest poultry processors in Brazil are expected to account for nearly 56 percent of total broiler slaughter, up from 55 percent in 2000, reflecting some consolidation in the sector. These same companies are also leaders in pork production in Brazil, which allows for economies of scale and greater use of lower-cost feeds based on volume purchases. Also, these large companies import corn under the draw-back system, which allows for exemption of import duties (10.5 percent) normally applied to corn imports from outside the MERCOSUL trading block. However, under this system, poultry processors must prove that corn imported will be used for processing products for export.

The following table provides an overview of the ten largest poultry processors in Brazil and their share in poultry production and exports, during 2000/01:

Company	Percent of tota	•	Percent of total exports		
	2000	2001	2000	2001	
Sadia	11.8	11.7	28.7	26.8	
Perdigao	9.0	10.1	21.3	18.6	
Doux-Frangosul	6.1	6.5	12.8	17.2	
Seara	5.5	5.8	17.2	17.2	
Avipal	4.2	4.4	1.2	2.7	

GAIN Report #BR2611 Page 8 of 11

Pena Branca	3.4	3.0	0.3	1.5
Dagranja	2.9	2.9	0.6	0.1
Chapeco	2.7	3.1	5.8	6.2
Aurora	2.7	2.2	2.2	2.0
Minuano	1.1	0.9	2.3	1.6

Source: Brazilian Poultry Exporters Association (ABEF)

## **Commodity Outlook, Turkey**

#### **Production**

Note: There are no official data on turkey production in Brazil. Data provided in this report are derived from interviews with sources from SADIA which accounts for slightly over 90 percent of turkey production in Brazil.

Brazilian turkey production is estimated to increase by nearly 10 percent in 2003, reflecting higher productivity, firm demand from the export market, and new investments in the Batavia poultry company. Batavia was purchased by PERDIGAO, the second largest poultry producer in Brazil and SADIA's main competitor. In addition, the French Company Doux Frangosul began production and marketing of its turkey line. In Brazil, the company will focus on turkey parts and products, instead of whole turkeys, and will concentrate on sales in the Brazilian market.

#### Consumption

Frozen Ready to Cook (RTC) turkey consumption remains highly seasonal in Brazil. Trade sources estimate that 85 percent of whole turkey sales occur during the pre-Christmas period, because consumer habits in Brazil favor turkey consumption during this holiday season. However, processed turkey products, such as sliced loaf and nuggets are consumed throughout the year. This is part of Sadia's business strategy to increase consumption of processed turkey products and to expand consumption of whole turkeys during other major holidays in Brazil.

#### **Trade**

Turkey exports are expected to continue to increase in 2003, after an-all time export record estimated for this year. During Jan-Jun 2002, turkey exports in volume increased by 9 percent compared to the same period last year, which reflects the competitiveness of the Brazilian product due to the recent devaluation of the "Real" and continued increase in turkey exports to the European Union.

<u>GAIN Report #BR2611</u> Page 9 of 11

**PSD Tables** 

# Poultry Meat, Chicken - 16 wks

PSD Table						
Country	Brazil					
Commodity	Poultry, Meat,	Broiler			(1000 MT)(M	IIL HEAD)
	Revised	2001	Preliminary	2002	Forecast	2003
	Old	New	Old	New	Old	New
Market Year Begin		01/2001		01/2002		01/2003
Inventory (Reference)	31	31	0	31	0	0
Slaughter (Reference)	3509	3509	0	3685	0	0
Beginning Stocks	170	170	196	0	120	0
Production	6580	6567	7040	7040	0	7180
Whole, Imports	0	0	0	0	0	0
Parts, Imports	0	0	0	0	0	0
Intra EC Imports	0	0	0	0	0	0
Other Imports	0	0	0	0	0	0
TOTAL Imports	0	0	0	0	0	0
TOTAL SUPPLY	6750	6737	7236	7040	120	7180
Whole, Exports	580	580	700	538	0	580
Parts, Exports	686	686	730	712	0	620
Intra EC Exports	0	0	0	0	0	0
Other Exports	10	0	12	0	0	0
TOTAL Exports	1266	1266	1430	1250	0	1200
Human Consumption	5288	5471	5686	5790	0	5980
Other Use, Losses	0	0	0	0	0	0

GAIN Report #BR2611 Page 10 of 11

Total Dom. Consumption	5288	5471	5686	5790	0	5980
TOTAL Use	6554	6737	7116	7040	0	7180
Ending Stocks	196	0	120	0	0	0
TOTAL DISTRIBUTION	6750	6737	7236	7040	0	7180
Calendar Yr. Imp. from U.S.	0	0	0	0	0	0

## Poultry meat, Turkey

PSD Table							
Country	Brazil						
Commodity	Poultry, Meat,	Turkey			(1000 MT)(M	(1000 MT)(MIL HEAD)	
	Revised	2001	Preliminary	2002	Forecast	2003	
	Old	New	Old	New	Old	New	
Market Year Begin		01/2001		01/2002		01/2003	
Inventory (Reference)	0	0	0	0	0	0	
Slaughter (Reference)	0	0	0	0	0	0	
Beginning Stocks	0	0	0	0	0	0	
Production	165	165	175	182	0	200	
Whole, Imports	0	0	0	0	0	0	
Parts, Imports	0	0	0	0	0	0	
Intra EC Imports	0	0	0	0	0	0	
Other Imports	0	0	0	0	0	0	
TOTAL Imports	0	0	0	0	0	0	
TOTAL SUPPLY	165	165	175	182	0	200	
Whole, Exports	2	3	3	3	0	3	
Parts, Exports	67	66	71	72	0	78	
Intra EC Exports	0	0	0	0	0	0	
Other Exports	0	0	0	0	0	0	
TOTAL Exports	69	69	74	75	0	81	
Human Consumption	96	96	101	107	0	119	
Other Use, Losses	0	0	0	0	0	0	

GAIN Report #BR2611 Page 11 of 11

Total Dom. Consumption	96	96	101	107	0	119
TOTAL Use	165	165	175	182	0	200
Ending Stocks	0	0	0	0	0	0
TOTAL DISTRIBUTION	165	165	175	182	0	200
Calendar Yr. Imp. from U.S.	0	0	0	0	0	0